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State of Idaho

Legislative Services Office

Individual Entity Audit Report

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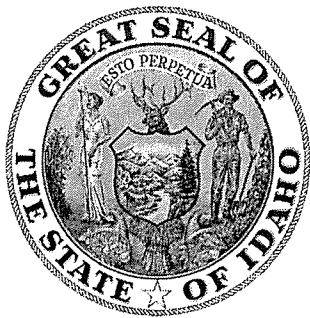
A communication to the Joint Finance-Appropriations Committee

**IDAHO STATE BOARD OF CORRECTION  
CORRECTIONAL INDUSTRIES**

**FY 2006 and 2007**

**Report OP23107  
Date Issued: July 3, 2008**

*Serving Idaho's Citizen Legislature*



Don H. Berg, Manager

Idaho Legislative Services Office  
Legislative Audits Division

**IDAHO STATE BOARD OF CORRECTION  
CORRECTIONAL INDUSTRIES**

## **SUMMARY**

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### **PURPOSE OF AUDIT REPORT**

We have audited the financial statements of the Idaho State Board of Correction, Correctional Industries for the fiscal years ended June 30, 2006 and 2007, in accordance with auditing standards generally accepted in the United States of America. The purpose of our audit is to determine whether Correctional Industries' financial statements are materially accurate and reliable, and that it complied with laws and regulations affecting fiscal operations.

### **CONCLUSION**

We conclude that Correctional Industries' financial statements are materially accurate and reliable, and fiscal operations materially comply with related laws and regulations. As a result, we issued an unqualified opinion on Correctional Industries' financial statements.

### **FINDINGS AND RECOMMENDATIONS**

There is one finding and recommendation in this report.

- 1) Material errors in the financial statements and other accounting errors were not detected by Correctional Industries' internal control procedures.

The complete finding is detailed on page 14. A copy of the entire report is available at <http://www.legislature.idaho.gov/audit/index.htm> or by calling 208-334-4832.

### **PRIOR FINDINGS AND RECOMMENDATIONS**

The prior report covered fiscal years 2004 and 2005, and included one finding and recommendation. As discussed below, the recommendation was implemented, and the finding is closed.

- 1) Correctional Industries has no policy and, in some instances, no support for allowances and other reserves.

We recommended that Correctional Industries review its accounting for allowances and reserves, and develop a policy for determining all allowances and reserves. The policy should explain when the allowances will be increased and decreased, as well as the basis for these increases and decreases. Compliance with its policy should be regularly monitored.

Correctional Industries has developed policies for its allowances and reserves, and is properly accounting for both. It is also monitoring and evaluating the allowances and reserves on an annual basis according to its policies. **CLOSED**

**AGENCY RESPONSE**

Correctional Industries has reviewed the report and is in general agreement with its contents.

**OTHER INFORMATION**

We discussed other issues which, if changed, would improve internal control, compliance, and efficiency.

This report is intended solely for the information and use of the State of Idaho and the Idaho State Board of Correction, Correctional Industries, and is not intended to be used by anyone other than these specified parties.

We appreciate the cooperation and assistance given to us by the general manager, Martin Thomas, and his staff.

**ASSIGNED STAFF**

Chris Farnsworth, CPA, Managing Auditor

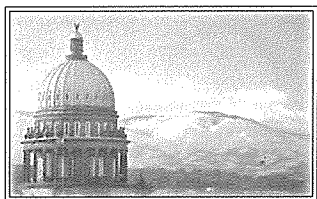
J.E. Bowden, CPA, Staff Auditor

Brian Butkus, Staff Auditor

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# Legislative Services Office Idaho State Legislature

*Serving Idaho's Citizen Legislature*

**Jeff Youtz**  
Director

June 12, 2008

Unqualified Opinion on  
Basic Financial Statements

## Independent Auditor's Report

Martin Thomas, General Manager  
Correctional Industries  
1301 N. Orchard Street, Suite 110  
Boise, ID 83706

Robin Sandy, Chair  
Board of Correction  
1301 N. Orchard Street, Suite 110  
Boise, ID 83706

Dear Mr. Thomas and Ms. Sandy:

We have audited the accompanying basic financial statements of the Idaho State Board of Correction, Correctional Industries, as of and for the years ended June 30, 2006 and 2007, as listed in the table of contents. These financial statements are the responsibility of Correctional Industries' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities of Correctional Industries as of June 30, 2006 and 2007, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 12, 2008, on our consideration of Correctional Industries' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered when assessing the results of our audit.

**Mike Nugent, Manager**  
Research & Legislation

**Cathy Holland-Smith, Manager**  
Budget & Policy Analysis

**Don H. Berg, Manager**  
Legislative Audits

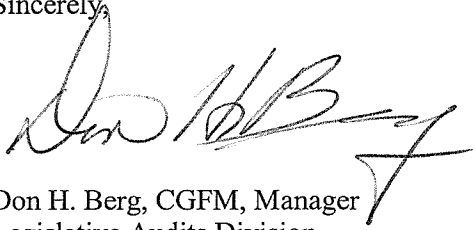
**Glenn Harris, Manager**  
Information Technology

Statehouse, P.O. Box 83720  
Boise, Idaho 83720-0054

Tel: 208-334-2475  
[www.legislature.idaho.gov](http://www.legislature.idaho.gov)

Correctional Industries has not presented the Management Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Sincerely,

A handwritten signature in dark ink, appearing to read "Don H. Berg", with a stylized flourish extending from the end.

Don H. Berg, CGFM, Manager  
Legislative Audits Division

STATE OF IDAHO  
CORRECTIONAL INDUSTRIES  
STATEMENT OF NET ASSETS  
AS OF JUNE 30, 2006 AND 2007

	Enterprise Fund	
	<u>June 30, 2006</u>	<u>June 30, 2007</u>
ASSETS		
Current Assets		
Cash	\$3,483,187	\$3,128,639
Investment (CD)	0	1,013,283
Accounts Receivable, Net	666,590	796,463
Prepaid Expenses	67,662	140,433
Inventory, Net	1,070,137	2,065,968
Construction in Progress	12,590	76,044
Total Current Assets	<u>\$5,300,166</u>	<u>\$7,220,830</u>
Non-current Assets		
Capital Assets, Net	<u>\$1,029,050</u>	<u>\$1,092,461</u>
Total Assets	<u><u>\$6,329,216</u></u>	<u><u>\$8,313,291</u></u>
LIABILITIES		
Current Liabilities		
Accounts Payable	\$324,018	\$260,856
Other Payables	47,463	46,290
Payroll and Benefits Payable	70,014	75,050
Compensated Absences Payable	42,927	52,688
Warranty and Showroom Reserve	8,885	8,578
Unearned Revenue	4,918	56,761
Total Current Liabilities	<u>\$498,225</u>	<u>\$500,223</u>
Non-current Liabilities		
Compensated Absences Payable	<u>\$52,467</u>	<u>\$64,396</u>
Total Liabilities	<u>\$550,692</u>	<u>\$564,619</u>
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	\$1,029,050	\$1,092,461
Unrestricted	<u>4,749,474</u>	<u>6,656,211</u>
Total Net Assets	<u>\$5,778,524</u>	<u>\$7,748,672</u>
Total Liabilities and Net Assets	<u><u>\$6,329,216</u></u>	<u><u>\$8,313,291</u></u>

The accompanying notes are an integral part of these financial statements.

STATE OF IDAHO  
CORRECTIONAL INDUSTRIES  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2006 AND 2007

	Enterprise Fund	
	<u>June 30, 2006</u>	<u>June 30, 2007</u>
OPERATING REVENUES		
Sales	\$7,344,031	\$8,611,933
PIE Program Sales	360,330	0
Total Operating Revenues	<u>\$7,704,361</u>	<u>\$8,611,933</u>
OPERATING EXPENSES		
Cost of Goods Sold	\$3,324,897	\$3,972,078
Personnel Costs	1,883,518	1,867,759
Indirect Inmate Labor	95,854	125,663
Travel and Training	23,675	25,107
Supplies	49,341	69,210
Depreciation Expense	163,289	173,460
Building, Equipment, and Maintenance	234,933	282,182
Utilities	180,061	134,718
Advertising, Insurance, and Professional Fees	55,062	64,584
Other Expenses	152,446	146,541
Write-Down of Inventory Value	906	2,981
PIE Program Expenses	360,330	0
Total Operating Expenses	<u>\$6,524,312</u>	<u>\$6,864,283</u>
Operating Income	<u>\$1,180,049</u>	<u>\$1,747,650</u>
NON-OPERATING REVENUES (EXPENSES)		
Interest Revenue	<u>\$102,385</u>	<u>\$180,189</u>
Total Non-Operating Revenues (Expenses)	<u>\$102,385</u>	<u>\$180,189</u>
NET INCOME (LOSS) BEFORE DISCONTINUED OPERATIONS	\$1,282,434	\$1,927,839
DISCONTINUED OPERATIONS		
Gain from Discontinued Operations	<u>0</u>	<u>42,309</u>
INCREASE IN NET ASSETS	\$1,282,434	\$1,970,148
BEGINNING NET ASSETS	<u>4,496,090</u>	<u>5,778,524</u>
ENDING NET ASSETS	<u><u>\$5,778,524</u></u>	<u><u>\$7,748,672</u></u>

The accompanying notes are an integral part of these financial statements.

STATE OF IDAHO  
CORRECTIONAL INDUSTRIES  
STATEMENT OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2006 AND 2007

	Enterprise Fund	
	<u>June 30, 2006</u>	<u>June 30, 2007</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash Received from Customers and Other Departments	\$7,727,637	8,601,267
Cash Payments to Suppliers for Goods and Services	(4,326,334)	(6,076,838)
Cash Payments to Employees for Services	(1,935,702)	(1,841,033)
Net Cash Provided by Continuing Operating Activities	\$1,465,601	683,396
Net Cash Provided by Discontinued Operating Activities	0	20,999
Net Cash Provided by Operating Activities	<u>\$1,465,601</u>	<u>704,395</u>
<b>CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES</b>		
Cash Proceeds from the Sale of Capital Assets	\$0	\$69,879
Cash Payments for Purchase of Capital Assets	(164,044)	(295,728)
Net Cash used by Capital Financing Activities	<u>(\$164,044)</u>	<u>(\$225,849)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Cash invested in Certificate of Deposit	\$0	(\$1,013,283)
Cash Received for Interest	102,385	180,189
Net Cash Provided (used) by Investing Activities	<u>\$102,385</u>	<u>(\$833,094)</u>
Net Increase (Decrease) in Cash	\$1,403,942	(\$354,548)
Cash at Beginning of Year	2,079,245	3,483,187
Cash at End of Year	<u>\$3,483,187</u>	<u>\$3,128,639</u>
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>		
Operating Income From Operating Activities	\$1,180,049	\$1,747,650
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:		
Depreciation Expense	163,290	173,460
Changes in Accounts Receivable	(78,918)	(129,873)
Change in Prepaid Expense	(60,139)	(72,771)
Changes in Inventory	315,489	(922,233)
Changes in Construction in Progress	69,800	(63,454)
Changes in Payables	(123,970)	13,926
Gain on Discontinued Operations	0	42,309
Net Cash Provided (Used) By Operating Activities	<u>\$1,465,601</u>	<u>\$704,396</u>

The accompanying notes are an integral part of these financial statements.

# NOTES TO THE FINANCIAL STATEMENTS FOR FISCAL YEAR 2006 AND 2007

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## NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

### **Financial Reporting Entity**

Correctional Industries' financial statements have been prepared in conformity with United States generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant Correctional Industries' accounting policies are described below.

Correctional Industries is established by Idaho Code and reports to the Idaho State Board of Correction.

Correctional Industries contributes to the cost-sharing, multi-employer Public Employee Retirement System of Idaho (PERSI). PERSI is administered by the State of Idaho, and Correctional Industries is not the major participant in the plan; therefore, the plan's financial statements are not included in this report.

### **Basis of Presentation**

Enterprise Fund Financial Statements – Correctional Industries is a government entity engaged in business-type activities. The Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Fund Net Assets; and the Statement of Cash Flows display information about Correctional Industries' financial operations for the years ended June 30, 2006 and 2007. These statements include all financial activity of Correctional Industries. These activities are financed primarily by fees charged for goods provided to customers. Such fees are classified as operating revenues. All other revenue is classified as non-operating.

### **Measurement Focus and Basis of Accounting**

Enterprise funds, in accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, are required to apply applicable GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements: *Statements and Interpretations of Financial Accounting Standards Board (FASB)*; *Accounting Principles Board Opinions*; and *Accounting Research Bulletins of the Committee on Accounting Procedure*. In addition, an enterprise activity may apply all FASB statements and interpretations issued after November 30, 1989, except those that conflict with or contradict GASB pronouncements. Correctional Industries has elected not to follow FASB pronouncements issued after November 30, 1989.

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. All assets and liabilities are presented in the Statement of Net Assets. Revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place.

**Cash**

Cash represents Correctional Industries' interest in an internal investment pool maintained by the State. The State Treasurer is the investment officer for the money on deposit in the State treasury. Idaho Code, Sections 67-1210 and 67-1210A, governs investment policies of the State Treasurer. Interest earned on Correctional Industries' portion of the investment pool is credited to Correctional Industries.

**Accounts Receivable**

Receivables consist primarily of the sale of goods to customers and are referred to as "trade receivables." Trade receivables are accounted for net of an allowance for doubtful accounts. Below is a schedule of receivable balances at June 30, 2006 and 2007.

	Accounts Receivable	Allowance for Doubtful Accounts	Net Accounts Receivable
Trade Receivables			
FY 2006	\$681,586	\$14,996	\$666,590
FY 2007	809,393	12,930	796,463

**Inventory**

Inventory consists of raw materials and supplies, work-in-process, and finished goods. Raw materials and supplies are valued at cost, less a reserve of \$58,064 for obsolete items. Correctional Industries has established a reserve for finished goods in the amount of \$9,294. Correctional Industries estimates that the cost, less the reserve, approximates market value. Work-in-process inventory is carried at actual accumulated cost. Finished goods inventory is carried at standard costs, with any actual cost variance expensed at the time of production.

**Capital Assets**

Capital assets are reported at cost, less any accumulated depreciation. Only assets with a value of \$5,000 or greater are capitalized. Depreciation is recorded by use of the straight-line method over a pre-determined useful life as shown below.

Assets	Years
Buildings	40
Improvements Other Than Buildings	10-40
Machinery, Equipment and Vehicles	3-5

Correctional Industries paid for the construction of some buildings. The value of these buildings is included in the financial statements as capital assets and is depreciated over a 40-year period. Some buildings are provided by the Department of Correction. The value of these buildings is not included in Correctional Industries' financial statements. Correctional Industries does not pay the Department of Correction for use of these buildings.

Correctional Industries is also in the process of expanding into the South bay of Building 23, upgrading its computer networking system, purchasing a CNC router, and updating its drafting facilities.

Schedules of capital assets at June 30, 2006 and 2007 are shown below.

<u>Fiscal Year 2006</u>				
	Beginning Balance	Additions	Retirements	Ending Balance
Assets				
Building – Depreciable	\$1,081,731	\$6,455	\$0	\$1,088,186
Equipment – Depreciable	1,902,804	157,623	(34)	2,060,393
Total Historic Cost	\$2,984,535	\$164,078	(\$34)	\$3,148,579
Less Accumulated Depreciation				
Buildings	(\$515,427)	(\$46,967)	\$0	(\$562,394)
Equipment	(1,440,812)	(116,322)	0	(1,557,134)
Total Accumulated Depreciation	(\$1,956,239)	(\$163,289)	\$0	(\$2,119,528)
Net Capital Assets	\$1,028,296	\$789	(\$34)	\$1,029,050

<u>Fiscal Year 2007</u>				
	Beginning Balance	Additions	Retirements	Ending Balance
Assets				
Building – Depreciable	\$1,088,186	\$24,001	\$0	\$1,112,187
Equipment – Depreciable	2,060,393	229,036	(108,426)	2,181,003
Total Historic Cost	\$3,148,579	\$253,037	(\$108,426)	\$3,293,190
Less Accumulated Depreciation				
Buildings	(\$562,395)	(\$47,299)	\$0	(\$609,694)
Equipment	(1,557,134)	(126,150)	92,249	(1,591,035)
Total Accumulated Depreciation	(\$2,119,529)	(\$173,449)	\$92,249	(\$2,200,729)
Net Capital Assets	\$1,029,050	\$79,588	(\$16,177)	\$1,092,461

Maintenance and repairs are charged to operations as incurred. When capital assets are disposed of, accumulated depreciation is deducted from the original cost, and any gain or loss arising from its disposal is credited or charged to operations.

#### **Accounts Payable**

Accounts payable are vendor-payment transactions occurring after the June 30 fiscal year-end for goods and services received by Correctional Industries prior to June 30.

#### **Other Payables**

These amounts are comprised primarily of inmate payroll and related taxes.

#### **Warranty and Showroom Reserve**

This amount is an estimate of costs to repair product deficiencies after the products have been delivered to the customers.

**Net Assets**

Net assets represent the difference between assets and liabilities and are divided into three components: (1) invested in capital assets, net of related debt; (2) restricted; and (3) unrestricted.

1. Invested in capital assets, net of related debt, consist of: capital assets, net of accumulated depreciation and reduced by any outstanding notes or other loans attributable to acquisition, construction, or improvement of those assets.
2. Restricted assets have constraints placed on their use. These constraints may be externally imposed by creditors or grantors, or imposed by enabling legislation or other statutes. Correctional Industries has no restricted assets.
3. Unrestricted net assets consist of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt." Unrestricted assets are generally available for general operations.

**Budgets**

Idaho Code, Section 20-419 provides Correctional Industries with a perpetual appropriation; therefore, spending authority is not limited by the legislature.

**NOTE 2. DEPOSITS AND INVESTMENTS**

Correctional Industries participates in the State Treasurer's Pooled Idle Fund. The fund is an internal investment pool managed by the State Treasurer's Office on behalf of the participants. Money not needed to meet immediate operating obligations is invested in accordance with Idaho Code, Sections 67-120 and 67-1210A. Participation in the pool is involuntary. Idaho Code restricts the State Treasurer to certain types of investments. The Pooled Idle Fund is an unrated internal investment pool. The fair value of investments based on Correctional Industries' participation in the pool as of June 30, 2006 and 2007, is \$3,483,187 and \$3,128,639, respectively.

Correctional Industries purchased a certificate of deposit in February 2007, in the amount of \$1 million. The interest rate is 5.45%, and interest is deposited quarterly. The purchase was facilitated by the State Treasurer's Office. The value of the certificate at June 30, 2007 was \$1,013,283. The certificate of deposit matured on February 12, 2008. This certificate of deposit is subject to custodial credit risk.

**Credit Risk**

Custodial credit risk is the risk that in the event of a financial institution's failure, Correctional Industries' deposits may not be returned. The State Treasurer's Office does not have a formal policy to address custodial credit risk.

**Interest Rate Risk**

The State Treasurer does not have a formal investment policy limiting investment maturities as a means of managing exposure to fair value losses arising from increasing interest rates.

**NOTE 3. COMPENSATED ABSENCES**

State of Idaho employee benefits include vacation and sick leave allowances. Overtime may be earned under provisions of the Fair Labor Standards Act and State law. Overtime is commonly referred to as "compensatory time" or "comp time," since employees may take time off for the accrued overtime. For purposes of earning and accruing overtime, there are three general classes of employees.

1. Those who earn overtime at 1.5 times regular pay rates and may be paid for the overtime or take time off.
2. Those who earn overtime at the same rate as regular pay rates and may only take time off.
3. Those ineligible for overtime.

Under certain circumstances, employees eligible for overtime may accrue earned administrative leave on an hour-for-hour basis. Earned administrative leave is treated similarly to vacation leave but is not subject to any limitation. Upon termination, the following accrued leave balances are paid:

1. Vacation leave
2. Overtime for those eligible for payment
3. Earned administrative leave

All vacation and compensatory pay is accrued as a payroll liability in the financial statements when the benefit is incurred.

As of June 30, 2006 and June 30, 2007, the following are changes and values of leave accrued and used by employees of Correctional Industries:

Fiscal Year 2006		Fiscal Year 2007	
July 1, 2005	\$94,492	July 1, 2006	\$95,394
Increases	17,039	Increases	39,681
Decreases	(16,137)	Decreases	(17,991)
June 30, 2006	<u>\$95,394</u>	June 30, 2007	<u>\$117,084</u>

Of the total amount at June 30, 2006 and June 30, 2007, Correctional Industries estimates, based on past experience, that \$42,927 and \$52,688, respectively, is due within one year.

Additional post-employment benefits, other than pension benefits that are funded or partially funded by Correctional Industries, relate to health insurance. These include a retirees' health insurance subsidy for eligible retired members under the Public Employees Retirement System of Idaho (PERSI) and health insurance funded from a sick-leave reserve fund. The health insurance subsidy plan is primarily paid for by the retiree with a portion of the costs subsidized by the active employee plan. The sick-leave reserve fund is used to pay health insurance costs for the retiree based on the amount of unused accumulated sick leave at the date of retirement. Upon retirement, 50% of the unused sick-leave value, not to exceed 600 hours, is used by PERSI to purchase supplemental health insurance for the retiree.

#### **NOTE 4. PENSION PLAN**

PERSI, a cost-sharing multiple-employer public retirement system, was created by the Idaho State Legislature. It is a defined benefit plan requiring that both the member and the employer contribute. Designed as a mandatory system for eligible State and school district employees, the legislation provided for political subdivisions to participate by contractual agreement with PERSI.

After five years of credited service, members become fully vested in retirement benefits earned to date. Members are eligible for retirement benefits when they reach the age specified by their employment classification. For each year of credited service, the annual service retirement allowance is 2.0% or 2.3% (depending on employee classification) of the average monthly salary for the highest consecutive 42 months.

For the years ended June 30, 2006 and 2007, the required contribution rate for general employees was 10.39% and 6.223% of covered payroll for Correctional Industries and its employees, respectively. Correctional Industries' contributions required and paid were \$140,517 for fiscal year 2006, \$138,233 for fiscal year 2007.

#### **NOTE 5. OPERATING LEASES**

Correctional Industries committed to leases for office space and manufacturing equipment in fiscal year 2005. All leases expire at the end of fiscal year 2008. Future minimum lease payments are shown below.

Fiscal Year Ending June 30	Total
2007	\$69,762
2008	<u>62,381</u>
Total Minimum Future Payments	<u><u>\$132,143</u></u>

#### **NOTE 6. RISK FINANCING**

The State maintains a combination of commercial and self-insurance to cover the risk of loss to which it may be exposed. This is accomplished through the Risk Management Fund and Group Insurance Fund, as well as various outside insurance providers.

The Risk Management Fund manages property and general liability risk. The Fund also finances and accounts for risks not covered by Group Insurance and outside insurance providers. General liability claims are self-insured up to the Idaho Tort Claims Act maximum for each claim. Comprehensive collision and physical damage to covered vehicles are self-insured for replacement cost.

The Group Insurance Fund is used to account for and finance life, health, and disability insurance programs. Long-term disability benefits within Group Insurance are partially insured through other insurers.

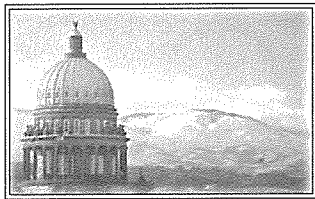
All State entities may participate in the Risk Management and Group Insurance programs. Payments are made to the Risk Management Fund based on actuarial estimates, loss experience, exposure, and asset value covered. Payments made to the Group Insurance Fund are based on actuarial estimates of the amounts needed to pay for negotiated coverage, based on projected claims experience.

#### **NOTE 7. GAIN FROM SALE OF ASSETS FROM DISCONTINUED OPERATIONS**

In the Spring of 2006, the Department of Correction decided to discontinue the garment shop operations. As a result, Correctional Industries recognized a gain of \$42,309 in fiscal year 2007.

#### **NOTE 8. RELATED-PARTY TRANSACTIONS**

Some buildings are provided by the Department of Correction. The value of these buildings is not included in Correctional Industries' financial statements. A Correctional Industries employee completes some work for the Department of Correction. Correctional Industries receives no compensation from the Department of Correction for the work of this employee.



# Legislative Services Office Idaho State Legislature

*Serving Idaho's Citizen Legislature*

**Jeff Youtz**  
Director

June 12, 2008

Independent Auditor's Report on Internal Control  
Over Financial Reporting and on Compliance and  
Other Matters Based on an Audit of Financial  
Statements Performed in Accordance  
With Government Auditing Standards

Martin Thomas, General Manager  
Correctional Industries  
1301 N. Orchard Street, Suite 110  
Boise, ID 83706

Robin Sandy, Chair  
Board of Correction  
1301 N. Orchard Street, Suite 110  
Boise, ID 83706

Dear Mr. Thomas and Ms. Sandy:

We have audited the financial statements of the Idaho State Board of Correction, Correctional Industries as of and for the years ended June 30, 2006 and 2007, and have issued our report thereon dated June 12, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

## Internal Control Over Financial Reporting

In planning and performing our audit, we considered Correctional Industries' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not for the purpose of expressing an opinion on the effectiveness of Correctional Industries' internal control. Accordingly, we do not express an opinion on the effectiveness of Correctional Industries' internal control.

Our consideration of the internal control was for the limited purpose described in the preceding paragraph, and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiency in internal control that we consider to be a significant deficiency and a material weakness.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote

**Mike Nugent, Manager**  
Research & Legislation

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Budget & Policy Analysis

**Don H. Berg, Manager**  
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Information Technology

likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

We have included one finding and recommendation in this report, and we consider the finding to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We consider the significant deficiency described in the included finding to be a material weakness.

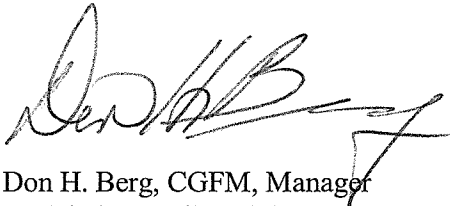
#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether Correctional Industries' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain other matters that we have reported to the management of Correctional Industries in a separate letter.

This report is intended solely for the information and use of the State of Idaho, the Idaho State Board of Correction, and Correctional Industries, and is not intended to be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in dark ink, appearing to read 'Don H. Berg', with a stylized flourish at the end.

Don H. Berg, CGFM, Manager  
Legislative Audits Division

# FINDINGS AND RECOMMENDATIONS

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## **FINDING #1**

Material errors in the financial statements and other accounting errors were not detected by current internal control procedures.

Internal control procedures should be designed to detect or prevent accounting errors and ensure that financial statements and other management reports are complete and accurate. We noted two significant errors and several lesser misstatements in the financial statements and other accounting errors that occurred due to incomplete or missing internal control procedures.

The significant errors involved \$360,000 in financial activity that was improperly excluded from the Statement of Revenues, Expenses, and Changes in Net Assets and the Statement of Cash Flows, and \$113,420 in financial activity that was improperly excluded on the Statement of Net Assets. Also, accounting errors resulted in receipts of \$427,000 being deposited in the wrong fund. This error resulted in three months of lost interest revenue of approximately \$3,500. Reconciliation procedures and management reviews should be enhanced or established to reduce the potential for errors to occur and go undetected.

Although the financial statements were corrected as a result of the audit, we are required under current auditing standards to report these weaknesses in internal control procedures.

## **RECOMMENDATION #1**

**We recommend that Correctional Industries enhance or establish internal control procedures over financial statement preparation and accounting procedures to reduce the potential for errors to occur and go undetected.**

### **AGENCY'S CORRECTIVE ACTION PLAN**

Three things caused these errors: PIE programs at ICC, an invoice paid in STARs that was not recorded in Great Plains, and deposits made into the incorrect cash fund account.

The PIE program at ICC is no longer active. This inactivity eliminates the need to create an internal control for this error.

CI is in the process of implementing a policy to ensure that the review of the Accounts Payable trial balance is performed accurately.

CI is in the process of implementing that cash reconciliation be performed within a specified time period. CI has also updated the procedure manual to include the correct fund in which to make deposits.

# AGENCY RESPONSE

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June 2, 2008

Mr. Don Berg  
Legislative Services Office  
Statehouse  
PO Box 83720  
Boise, Idaho 83720-0054

**Subject** Audit Findings and Recommendations Status

**Finding #1. Material errors in the financial statements and other accounting errors were not detected by current internal control procedures.**

**Recommendation #1.** We recommend that Correctional Industries enhance or establish internal control procedures over financial statement preparation and accounting procedures to reduce the potential for errors to occur and to undetected.

**CI Corrective Action Plan.** Three things caused these errors. PIE programs at ICC, an invoice paid in STARS, which was not recorded in Great Plains, and deposits made into the incorrect cash fund account.

The PIE program at ICC is no longer active. This inactivity eliminates the need to create an internal control for this error.

CI is in the process of implementing a policy to ensure that the review of the Accounts Payable trial balance is performed accurately.

CI is in the process of implementing that cash reconciliation be performed within a specified time period. CI has also updated the procedure manual to include the correct fund in which to make deposits.

**Status. In process**

Sincerely,

Martin Thomas  
General Manager

# APPENDIX

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## **HISTORY**

The 1974 Idaho Legislature passed the Correctional Industries Act, creating the Correctional Industries Commission to oversee a manufacturing entity exempt from many State regulations. Prior to that time, the manufacturing entity operated as productive enterprises in prison facilities.

The manufacturing entity operated in this manner until 1980. At that time, the Correctional Industries Commission was abolished, and the Board of Correction assumed supervisory responsibility. The financial affairs of Correctional Industries were also moved from a private bank account to an account in the Office of the State Treasurer. The records of receipts and expenditures are kept by the Office of the State Controller.

## **STATUTORY AUTHORITY**

The statutory authority for Correctional Industries is found in Chapter 4, Title 20 of the Idaho Code.

Statutory authority allows the Board to enter into contracts and agreements (Idaho Code, Section 20-408), and exempts Correctional Industries from powers and duties of the State purchasing agent (Idaho Code, Section 20-416).

## **PURPOSE**

The general purpose of Correctional Industries is to provide opportunities for incarcerated persons to obtain job skills and develop positive work attitudes.

The mission of Correctional Industries is multifaceted: first, to reduce inmate idleness by employing inmates through safe, productive, and rehabilitative training and employment enterprises, which should teach valuable job-seeking and job-keeping skills; second, to produce and market modern, cost-effective, quality products and services at competitive prices to meet the needs of authorized markets; and third, to save taxpayer dollars and raise sufficient revenue to sustain operating costs of Correctional Industries' programs and help offset costs of future expansion.

## **FUNDING**

Correctional Industries is funded primarily by revenue generated from the sale of merchandise. Merchandise currently produced and sold includes license plates, signs, furniture, and various custom-built projects requiring skills in metalwork, upholstery, and carpentry.

## **ORGANIZATION**

Correctional Industries is a division of the Department of Correction. Correctional Industries' daily operations are supervised by a general manager and organized into four functional areas: (1) accounting and administration, which provides accounting, purchasing, and business management services to the other divisions; (2) sales and marketing, which provides sales support and research into new product lines; (3) production, which provides manufactured goods for sale; and (4) transportation, which ensures delivery of goods to purchasers.

Correctional Industries operates the following shops:

**Print and Sign Shops**

- Print Shop: Offers complete printing services, including design, layout, production, and delivery.
- Sign Shop: Produces various traffic, informational, and miscellaneous signs.

**Metal Shop**

- Produces metal products for a wide variety of users and specializes in detention furniture, bunks, tables, and storage units.

**Tag Shop**

- Produces authorized State of Idaho license plates for automobiles, trailers, recreation vehicles, and commercial trucks, as well as a complete line of personalized plates.

**Furniture Shops**

- Drafting Shop: Provides furniture and panel system designs for Correctional Industries.
- Carpentry Shop: Produces a large volume of standard wood office products; specializes in solid oak desks, bookcases, credenzas and accessories.
- Upholstery Shop: Produces a standard line of office chairs and seating; reupholsters and restores existing furniture.
- Panel Shop: Offers large-scale, custom carpentry and piecework on special design furniture projects; builds and installs systems furniture, including design, layout, and production.

**Decal Shop**

- Produces State-authorized decals for validation and registration of boats, vehicles, and trailers.

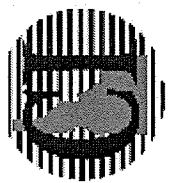
**Garment Shop**

- Produced inmate clothing for sale to the Department of Correction and local jails. This shop was discontinued in fiscal year 2007.

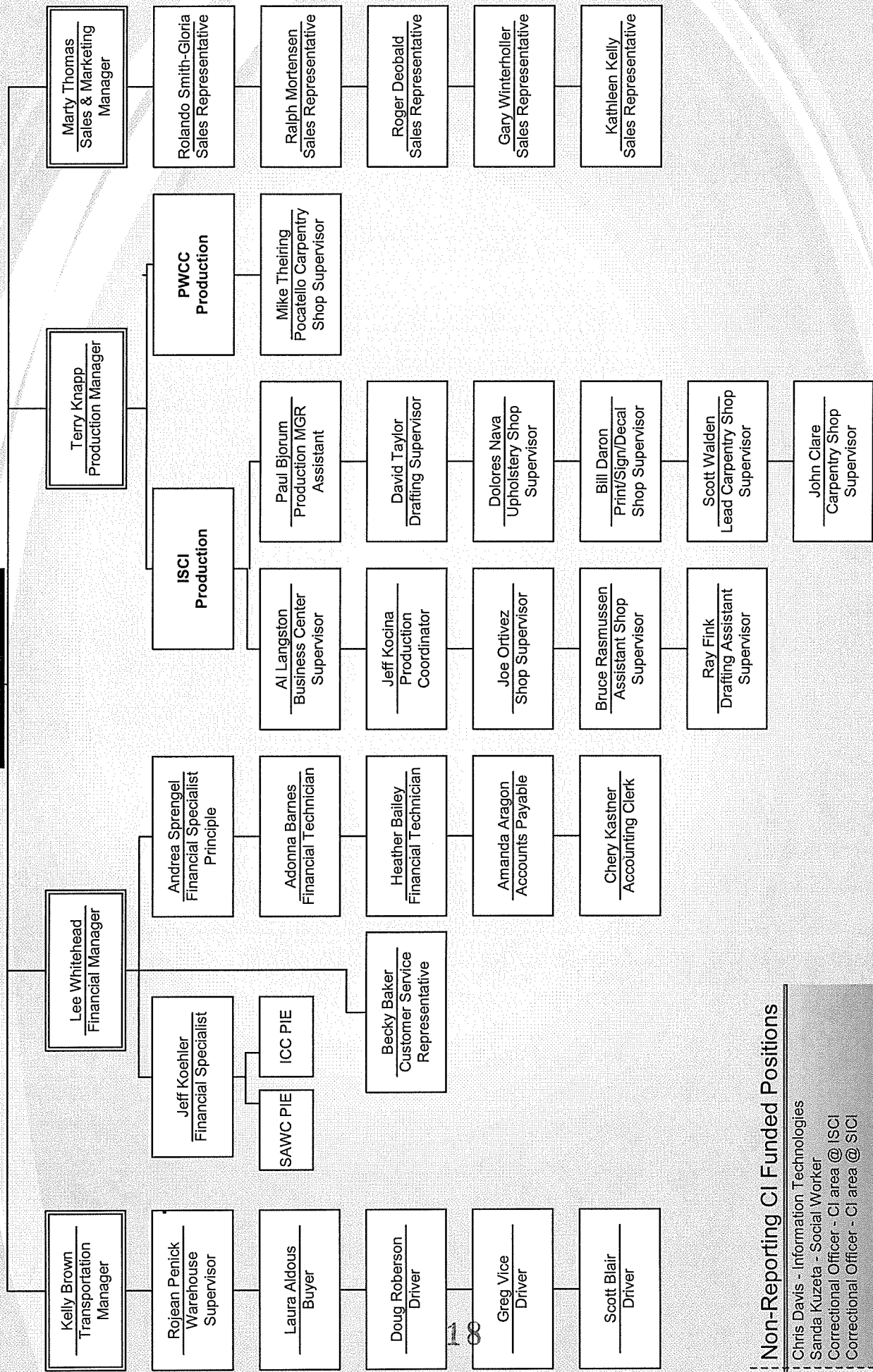
**Prison Industries Enhancement Certification Program**

- Provides workforce to the private sector at federal minimum wage and higher.

Correctional Industries' organizational chart is on the following page.



# Correctional Industries Organizational Chart



## Non-Reporting CI Funded Positions

Chris Davis - Information Technologies  
Sanda Kuzeta - Social Worker  
Correctional Officer - CI area @ ISCI  
Correctional Officer - CI area @ SICI